**MMN BINA SDN BHD**

**v.**

**FELDA PROPERTIES SDN BHD**

HIGH COURT MALAYA, KUALA LUMPUR
VARGHESE GEORGE JC
[ORIGINATING SUMMONS NO: D-24NCC-301-2010]
16 NOVEMBER 2010

***CONTRACT:*** *Guarantee - Bank guarantee - Demand on guarantee - Whether unconscionable - Whether ground for allowing restraining order - Whether unconscionable act proved on facts*

***BANKING:*** *Performance bonds - Beneficiary's right - Call on bond - Whether unconscionable - Whether ground for allowing restraining order - Whether unconscionable act proved on facts*

The plaintiff was the defendant's contractor for the construction and completion of a project for a contract value of RM19,750,000 (the 'contract'). As part of the contract, the plaintiff provided a bank guarantee by CIMB Bank Berhad ('BG') for the due performance of the contract in the sum of 5% of the consideration of the contract. The BG, in the sum of RM987,750 ('BG'), was dated 29 July 2008 and the defendant was named as the beneficiary of the guaranteed sum. A dispute arose between the parties with the plaintiff claiming that the work under the contract was completed, making references to various letters from the defendant's engineer in June 2008 and July 2008 in support thereof. However, the plaintiff admitted that certain remaining works and rectification to defects maintained by the defendant's engineer on 8 November 2008 were yet to be completed by the plaintiff as of that date. A joint inspection and survey was also held by both parties on 12 January 2009 but their disputes and differences continued to remain unresolved. Incidentally, their matter was not referred to arbitration as per cl. 55 of the contract. On 12 August 2010, the defendant made a demand on the BG and on 19 August 2010, the plaintiff was duly informed by CIMB Bank Berhad of the demand made and that the guaranteed sum would be paid within seven days thereof to the defendant. That resulted in the instant *ex parte* application filed by the plaintiff on 26 August 2010, *ie*, on the last day before the expiry of the seven-day period, for a restraining order against the defendant from making the said demand until further order of the court or until after the lapse of 84 days from the date of the

engineer's decision or in the event of an arbitration between the parties. The plaintiff's originating summons filed on 27 August 2010 also sought for the same restraining order. The plaintiff relied on the ground that the defendant's said demand was unconscionable in the circumstances of the case.

**Held (dismissing *ex parte* application and originating summons for restraining order):**

**(1)** There was no justification for the court to withhold assistance to a party who approached the court for intervention on the grounds of "unconscionability" or *mala fide* acts on the part of the beneficiary, which if refused, could result in similar or more severe damage and loss to the aggrieved party than in a "fraud" context. Although the unconscionability principle was an accepted additional exception and a sound principle of law in the Malaysian jurisdiction, but on the facts of the instant case, a case of unconscionable conduct on the defendant's part was not sufficiently made out for the court's intervention. (paras 11 & 12)

**(2)** There was nothing shown before the court that would prick the conscience of an ordinary man that the defendant's act was "unconscionable" when making the demand on the BG. The issues raised by the plaintiff were purely contractual issues and were not for the court to decide but for other forums pursuant to cl. 55 of the contract. The underlying contract between the parties formed no part of the BG. The findings of the engineer/arbitrator should not be pre-empted and the court should be vary to encroach onto the jurisdiction vested in them (*Cygal Bhd v. Bandar Subang Sdn Bhd*). There was also nothing to cast aspersions of bad faith on the defendant's conduct in making the demand on the BG. (paras 15 & 16)

**(3)** The balance of convenience test was not applicable in cases of irrevocable letters of credit or on demand performance bonds/guarantees. Any dispute between the parties would not affect the operation of the performance bond/guarantee (*LEC Contractors (M) Sdn Bhd v. Castle Inn Sdn Bhd & Anor*). In the circumstances of the case, the defendant, being the beneficiary of the "on-demand" and "unconditional" BG, could not and should not be restrained from receiving and dealing with the proceeds of the BG. (paras 17 & 19)

**Case(s) referred to:**

*Bocotra Construction Pte Ltd & Ors v. AG (No 2) [1995] 2 SLR 733* ***(refd)***
*Cygal Bhd v. Bandar Subang Sdn Bhd [2004] 3 CLJ 67 CA* ***(refd)***
*Edward Owen Engineering Ltd v. Barclays Bank International Ltd [1978] QB 159 CA* ***(refd)***
*Focal Asia Sdn Bhd & Anor v. Raja Noraini Raja Datuk Nong Chik & Anor [2009] 1 LNS 913 HC* ***(refd)***
*LEC Contractors (M) Sdn Bhd v. Castle Inn Sdn Bhd & Anor [2000] 3 CLJ 473 CA* ***(refd)***
*Nafas Abadi Sdn Bhd v. Putrajaya Holdings Sdn Bhd [2004] 1 LNS 127 HC* ***(refd)***
*Pasukhas Construction Sdn Bhd & Anor v. MTM Millenium Holdings Sdn Bhd & Anor [2009] 6 CLJ 480 HC* ***(refd)***
*Satriadesa Corporation Sdn Bhd v. Tenaga Nasional Bhd [2010] 4 CLJ 877 HC* ***(refd)***
*The Radio & General Trading Co Sdn Bhd v. Wayss & Freytag (Malaysia) Sdn Bhd [1997] 1 LNS 400 HC* ***(refd)***

*For the plaintiff/applicant - Steven How (Jasmine Chin with him); M/s Kumar Jaspal Quah & Aishah*
*For the defendant/respondent - Rajendra Kulasegaran; M/s Ranjit Thomas & Kula*

*Reported by Usha Thiagarajah*

## JUDGMENT

**Varghese George JC:**

**Grounds Of Decision**

**[1]** Enclosure 1 was an *ex parte* application by the plaintiff (by way of summons-in-chambers) filed on 26 August 2010 which essentially sought for a restraining order against the defendant from making a demand on a Bank Guarantee with the reference No. TF 001 G 8-247 given by CIMB Bank Berhad (hereinafter referred as 'the BG') until further order of the court, or till after the lapse of 84 days from the date of the decision of the 'engineer' or in the event of an arbitration between the parties, until an award is published thereunder, whichever was the later.

Enclosure 1 was supported by affidavit sokongan affirmed by one Nazrin b. Basri for the plaintiff (encl. 2).

**[2]** The originating process, namely, the saman pemula (encl. 4) was filed on 27 August 2010 seeking in effect the same restraining order.

**[3]** The material factual background upon which the application was made were as follows:

(a) The plaintiff had been engaged by the defendant, and by an agreement entered into on 20 October 2005 was the contractor for the construction and completion of a project known as "Cadangan Membina dan Menyiapkan Rumah Kos Rendah Setingkat, Rumah Kos Sederhana Setingkat, Kedai Setingkat, Pencawang Elektrik dan Kerja-Kerja Infrastruktur yang Berkaitan Di Felda Keratong 3, Mukim Keratong, Daerah Rompin, Pahang Darul Makmur" for a contract value of RM19,750,000 (hereinafter referred as 'the contract').

(b) It was a term of the contract that the plaintiff provides a guarantee for the due performance of the contract in the sum of 5% of the consideration of the contract. Accordingly there was in place the BG to the value of RM987,750. The BG which was dated 29 July 2008 named the defendant as the beneficiary to the guaranteed sum.

(c) The plaintiff claims that the works under the contract had been completed and in support of the same made reference to various letters from the defendant's engineer in June 2008 and July 2008. (paras. 9 of the affidavit sokongan).

(d) The BG, it must be noted however, was issued on 29 July 2008. It was also admitted by the plaintiff that the defendant's engineer had on 8 November 2008 maintained that certain remaining works and rectification to defects to have been undertaken by the plaintiff had not been completed by the plaintiff as of that date. It also appeared from the material before the court, that a joint inspection and survey had even been held by the parties on 12 January 2009 but the disputes and differences between the parties continued to remain unresolved.

(e) Neither the plaintiff nor the defendant had invoked cl. 55 of the contract to refer the differences and disputes as between them towards resolution by arbitration, in any event.

**[4]** On 12 August 2010, the defendant proceeded to issue a demand on CIMB for payment of the sum guaranteed under the BG. On 19 August 2010, the bank informed the plaintiff in writing that a demand had been received in respect of the BG from the defendant and that the bank would proceed to pay the sum in question within seven (7) days to the defendant.

Enclosure 1 was filed only on 26 August 2010 the last day before expiry of that seven day period.

**[5]** When the matter first came up before me on 27 August 2010, I directed that encl. 1 be served on the defendant and the plaintiff's application be disposed of *inter parte*.

On 30 August 2010 in the presence of both counsel for the plaintiff and the defendant, I granted an *ad interim* order and adjourned encl. 1 for hearing and disposal to 17 September 2010 to enable the counsel for the defendant to take further instructions and file any affidavit in reply.

**[6]** Before me, it was admitted and conceded by counsel for plaintiff that the BG in question was an 'on-demand' and 'unconditional' guarantee or bond. Clause 1 of the BG is set out below in any event for reference:

> 1. Apabila sahaja FPSB membuat tuntutan bertulis, maka Penjamin hendaklah dengan serta merta membayar kepada FPSB nilai yang ditentukan di dalam tuntuan tersebut *tanpa mengira samada terdapat apa-apa bantahan atau tentangan daripada Kontractor atau Penjamin atau mana-mana pihak ketiga yang lain dan tanpa bukti atau bersyarat.* Dengan syarat sentiasanya bahawa jumlah tuntutan yang dibuat tidak melebihi sebanyak Ringgit Malaysia: Sembilan Ratus Lapan Puluh Tujuh Ribu Tujuh Ratus Lima Puluh Sahaja (RM987,750.00) dan bahawa tanggungan Penjamin untuk membayar kepada FPSB di bawah Perjanjian ini tidak melebihi nilai tersebut di atas.

**[7]** Before me, it was also agreed by counsel for the plaintiff that the only recognized exception in law to the strict liability of banks or other issuers of on-demand or unconditional guarantees and bonds to pay on demand (and conversely for the beneficiary to receive the guaranteed sum) was where clear instance of 'fraud' had been shown and of which circumstances of fraud the bank or issuer had notice of as well. (*Edward Owen Engineering Ltd. v. Barclays Bank International Ltd* [1978] QB 159 CA; *LEC Contractors (M) Sdn Bhd v. Castle Inn Sdn Bhd & Anor* [2000] 3 CLJ 473 CA).

**[8]** Counsel for the plaintiff confirmed that he was not relying or raising any issue of 'fraud' on the part of the defendant as the basis of this application. He however went on to submit that 'unconscionability' on the part of the beneficiary in calling for payment on a performance guarantee is a separate and distinct

ground from fraud for seeking injunctive relief. In this case he submitted that he was only relying on 'unconscionability' on the part of the defendant in making the demand on the BG, as the sole ground for intervention sought of this court to make the orders prayed for against the defendant.

In support of his case he principally relied on the decision of the Singapore Court of Appeal in *Bocotra Construction Pte. Ltd. & Ors v. AG (No. 2)* [1995] 2 SLR 733 and referred to decisions of our High Court in:

(i) *Nafas Abadi Sdn Bhd v. Putrajaya Holdings Sdn Bhd* [2004] 1 LNS 127,

(ii) *The Radio & General Trading Co Sdn Bhd v. Wayss & Freytag (Malaysia) Sdn Bhd* [1997] 1 LNS 400) (Kamalanathan Ratnam J),

(iii) *Pasukhas Construction Sdn Bhd & Anor v. MTM Millenium Holdings Sdn Bhd & Anor* [2009] 6 CLJ 480 (Mohd. Hishamuddin J),

(iv) *Satriadesa Corporation Sdn Bhd v. Tenaga Nasional Bhd* [2010] 4 CLJ 877 (Prasad S Abraham JC),

as some Malaysian decisions which have recognized, if not applied, this principle of law that 'unconscionability' is an additional exception or separate ground for the courts to intervene and allow restraining orders where the interest of justice require it be done.

**[9]** In addition to the above Malaysian decisions, I need to also make reference the recent decision of Mohamad Ariff J in *Focal Asia Sdn Bhd & Anor v. Raja Noraini bt. Raja Datuk Nong Chik & Anor* (now reported in [2009] 1 LNS 913), where His Lordship made the following observation:

> The Singapore Court of Appeal in *Bocotra* … accepted the legal position that the court will grant an interlocutory injunction restraining a beneficiary from calling on the bond on the ground of fraud or unconscionability …
>
> In my view, the judicial and extra judicial views expressed in Singapore accord with good commercial sense, and unless precluded by higher authority and doctrine of precedents, I am of the opinion that this view point should be followed and adopted in Malaysia.

**[10]** Counsel for the defendant in respect of this issue of 'unconscionability' as a separate and distinct exception (that is, apart from fraud) laid emphasis on the judgment of Hishamudin Mohd. Yunus J in *Pasukhas Construction* case where His Lordship stated as follows:

> In the light of *Esso Petroleum Malaysia Inc* and *LEC Contractors*, I am not at liberty to apply the unconscionability principle as propounded by the Singapore Court of Appeal case of *Bocotra Construction*-although some of our High Court decisions that I have mentioned above have applied that principle. *Bocotra Construction*, being a decision of the Court of Appeal of Singapore is a persuasive authority; and the principle of unconscionability that it enunciated appears to me to be a sound principle. But, regrettably, I am bound by the doctrine of binding precedents. I am bound by the decision of the Supreme Court in *Esso Petroleum Malaysia Inc* (which applied the *American Cynamid* principles) or alternatively, by the Court of Appeal in *LEC Contractors* (which applied the fraud test).

**[11]** With reference to our Court of Appeal decision in LEC Contractors, as I have noted in another decision of mine *(Sumatec Engineering and Construction Sdn Bhd v. Malaysian Refining Company Sdn Bhd)*, our Court of Appeal may appear at first glance to be averse to 'unconscionability' being received or adopted here as a distinct ground for the court's intervention and this is usually attributed to the one sentence in the judgment there which reads: 'Bad faith or unconscionable conduct by itself is not fraud.'

However I would beg to state, on a full reading of that decision, that the focus of the learned judges appear to be on what constituted or did not constitute 'fraud' and whether it was pleaded in that particular case. As is accepted in law, 'fraud' would no doubt encompass some element of 'criminality' or deceit. 'Unconscionability', on the other hand, would not necessarily always amount to 'criminal' acts. I am of the view that there is no justification, in principle or policy, why the same assistance of the court should be withheld from a party who approaches the court for intervention on the grounds of 'unconscionability' or *mala fide* acts on the part of the beneficiary, which if refused, could result in similar or more severe damage and loss to the aggrieved party as would happen in a 'fraud' context.

As noted further in my decision there, which I reproduce here:

> I am of the view that where a demand is made by a beneficiary in respect of an unconditional guarantee or bond, the development of law should be in the direction of recognizing and accepting

A 'unconscionability' surrounding the demand or conduct of the party making the demand – as a further ground for intervention by the courts (in addition to the exception of 'fraud') to issue restraining orders in appropriate cases. Equity should come in and be unrestricted where the facts and circumstances require it to come to the aid of a party seeking justice.

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The availability of this further exception as an independent and separate one apart from fraud, however in my view, should be with one 'caveat', namely that there be placed before the court manifest or strong evidence of some degree in respect of the alleged 'unconscionable' circumstances or demand and not a bare statement or claim. However on the other hand it should not be too stringent and high as well, so as to stultify the equitable jurisdiction of the Court as observed by Mohamed Ariff, J, in *Focal Asia Sdn Bhd & Anor v. Raja Noraini Raja Datuk Nong Chick & Anor*. This additional exception should only be allowed with circumspect where events or conduct are of such degree such as to prick the conscience of a reasonable and sensible man.

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**[12]** Having said that although I am inclined to accept that additional exception as a sound principle of law in our jurisdiction, I was not however persuaded on the facts of this case as presented before this court, that a case of 'unconscionable' conduct on the part of the defendant had been sufficiently made out for the intervention of this court, in any event.

E

**[13]** Counsel for the plaintiff in his arguments highlighted the following as being the elements of 'unconscionability' in support of his case:

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(a) The contract had been substantially performed and only a dispute as to 'remedial' or rectification works and related costs remained outstanding. As such a 'termination' of the contract and the demand on the performance guarantee at this stage, it was alleged, was improper;

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(b) There were 'retention sums' still to be released to the plaintiff under the contract and such sums standing to the credit of the plaintiff should have been part utilized before the sum under the BG is demanded in any event by the defendant;

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(c) That the balance sum payable to the substitute contractor or contractor who had now been retained by the defendant to do the rectification or to complete the works (Netspek Sdn Bhd) was only about RM800,000, and this sum was well covered or secured by the 'retention sum' of RM987,810 still held by the defendant under the contract.

I

**[14]** Counsel for the defendant pointed out that, in any event, the contract had not been fully performed or completed. In the certification issued by the Engineer (Superintending Officer) referred to by the plaintiff's counsel, it was clearly stated that only 10% of the 'Testing and Commissioning' aspects of the contracted works had been completed with the remaining of that component of the work remaining outstanding. It was also submitted for the defendant that there were adequate grounds for the contract to be terminated and for the substitute contractor to be appointed. In other words the claim of the plaintiff that the contract had been performed was seriously disputed by the defendant and shown to be so on the material before the court.

**[15]** There was nothing shown to me which in my objective assessment, would prick the conscience of an ordinary man as amounting to an 'unconscionable' act or acts by the defendant when making the demand on the BG. The issues raised by the plaintiff were the normal issues that one sees in construction contract-disputes, like:

(1) whether the contract was duly discharged by performance;

(2) whether the contract was validly terminated;

(3) what would be the state of the final accounts as between the parties, in

all of which were not for this court to decide but for other forums pursuant to cl. 55 of the contract (as had been agreed by the parties when they entered into the relationship), namely, first at the 'engineer' level, and then if still not acceptable, by way of arbitration. *Ex facie*, there was nothing before me as well that appeared to cast any aspersions of bad faith or an unfair shade on the conduct of the defendant in making the demand on the BG.

**[16]** These were purely contractual issues between the parties on the terms of and applicability of the underlying contract between them. As observed by Gopal Sri Ram JCA (as His Lordship then was) in *Cygal Bhd v. Bandar Subang Sdn Bhd* [2004] 3 CLJ 67, the underlying contract forms no part of the performance bond/guarantee and breaches and dispute are subject matter of arbitration and this court should not pre-empt the engineer's/arbitrator's finding and should be wary to encroach onto the jurisdiction vested in them.

**[17]** Furthermore, our Court of Appeal in *LEC Contractors* has affirmed that 'balance of convenience test' (following *Bocotra*'s other area of decision) was not applicable in the cases of irrevocable letters of credit or on demand performance bonds/guarantees and any dispute between parties would not affect the operation of the performance bond/guarantee.

**[18]** I agreed with counsel for the defendant that in the circumstances of this instant case, the defendant, being the beneficiary of the 'on-demand' and 'unconditional' BG could not and should not be restrained in all the circumstances of the case from receiving and dealing with the proceeds of the BG.

**[19]** Accordingly, I dismissed encl. 1 and also struck out encl. 4 (the saman pemula – which was substantially for the same relief as in encl. 1). I also ordered that the *ad interim* order given on 30 August 2010 to be dissolved. The plaintiff was further ordered to pay the defendant costs which was fixed at RM8,000.